IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No. 113 of 1994
WITH
INCOME TAX REFERENCE NO. 11 OF 1994
AND
INCOME TAX REFERENCE NO.294 OF 1994

For Approval and Signature:

HONOURABLE MR.JUSTICE D.A.MEHTA
HONOURABLE MS.JUSTICE H.N.DEVANI

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1 Whether Reporters of Local Papers may be allowed to see the judgment ?

2 To be referred to the Reporter or not ?

3 Whether their Lordships wish to see the fair copy of the judgment ?

4 Whether this case involves a substantial question of law as to the interpretation of the constitution of India, 1950 or any order made thereunder ?

5 Whether it is to be circulated to the civil judge ?

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COMMISSIONER OF INCOME TAX - Applicant(s)

Versus

GUJARAT STATE EXPORT CORPN - Respondent(s)

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Appearance :
MRS.M.M. BHATT for applicant - revenue

MR.S.N.SOPARKAR, Sr. Advocate with MRS SWATI SOPARKAR for

the Respondent - assessee

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CORAM : HONOURABLE MR.JUSTICE D.A.MEHTA
and
HONOURABLE MS.JUSTICE H.N.DEVANI

Date : 23/08/2005

ORAL JUDGMENT

(Per : HONOURABLE MR.JUSTICE D.A.MEHTA)

1.The following common question of law has been referred by the Income Tax Appellate Tribunal, Ahmedabad Bench “A”, under Section 256(1) of the Income Tax Act, 1961 (the Act) at the instance of the Commissioner of Income Tax in all the three references. Therefore, all the three references have been heard together and are being disposed of by this common judgement and order.

> “Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that HPS groundnuts exported by the assessee did not come within the ambit of expression “agricultural primary commodities” in Section 80HHC(2)(b)(i) of the I.T. Act, 1961 and that deduction under Section 80HHC(i) of the Act was allowable?”

2.It is an accepted position between the parties that the lead matter is Income Tax Reference No.113 of

1994 and hence, the facts necessary for the determination of the question are taken from the said reference.

3. The assessment year is 1983-84 and the relevant accounting period is 31st December 1982. The assessee, a State Government Corporation is carrying on business of export of various commodities. A deduction was claimed under Section 80HHC of the Act, and the same was allowed by the assessing officer vide assessment order dated 17/3/1986 framed under Section 143(3) of the Act.

4. The Commissioner of Income Tax (CIT) initiated action under Section 263 of the Act and vide order dated 28/3/1988, after hearing the assessee, partially set aside the assessment order on the issue of deduction under Section 80HHC of the Act, by holding the original assessment order as being erroneous and prejudicial to the interests of the revenue.

5. The assessee carried the matter in appeal before

the Tribunal, who allowed the appeal of the assessee vide its order dated 1st April 1991. It is this order which is under challenge.

6. Mrs.M.M.Bhatt, the learned standing counsel for the applicant revenue submitted that the assessee had exported groundnuts which were agricultural primary commodity within the meaning of Section 80HHC(2)(b)(i) of the Act, and hence, the assessee was not entitled to deduction under Section 80HHC of the Act. Referring to the activities which were carried out by the assessee before exporting the goods, it was submitted that the characteristic of groundnuts remained the same and the processes undertaken by the assessee did not result in any new commodity. In other words, unshelled groundnuts, according to the learned counsel, did not get changed to other commodity when by the processes undertaken by the assessee only the kernels were exported after removing the shells. That agricultural produce was groundnut, it was agricultural primary commodity, and the commodity as such did not get converted into another

commodity, nor did it change its form and substance. She, therefore, urged that, in the circumstances, the impugned order of Tribunal was bad in law. In support of her submissions, she has placed reliance on the decisions of the Apex Court reported in Commissioner of Income Tax v. Cynamid India Ltd., [1999] 237 ITR 585 and The Belsund Sugar Co. Ltd. v. The State of Bihar, AIR 1999 SC 3125.

7. As against that, supporting the order of the Tribunal, Mr.S.N.Soparkar, the learned Senior Advocate appearing on behalf of the respondent, submitted that the Tribunal had recorded finding of fact that the goods exported by the assessee were not agricultural primary commodity once they had undergone the various processes which were noted by the Tribunal. It was submitted that the assessee, in support of its case, had furnished certificate of an expert in the field and there was no evidence to the contrary. That accordingly, the goods exported by the assessee ceased to be agricultural primary commodity and HPS groundnuts were known as

a different commodity in market. It was urged that the contention of revenue, if accepted, would mean that the word “primary” appearing in the phrase “agricultural primary commodities” had to be ignored. That there was a difference between a commodity which was a primary commodity and a secondary commodity or other commodity as distinguished from primary commodity. In this connection, he placed reliance on the Apex Court decisions in case of Commissioner of Income Tax v. Cynamid India Ltd. (supra) as well as Aspinwall & Co. Ltd. v. Commissioner of Income Tax, [2001] 251 ITR 323. He, therefore, urged that the Tribunal's order be upheld and the question be answered in favour of the assessee.

8. Section 80HHC, as was applicable for the three assessment years under consideration, and relevant for the present, reads as under :

> “**Deduction in respect of export turnover**.
>
> **80HHC**. (1) Where the assessee,

being an Indian company or a person (other than a company)who is resident in India, exports out of India during the previous year relevant to an assessment year any goods or merchandise to which this section applies, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, the following deductions, namely :-

(a) a deduction of an amount equal to one per cent of the export turnover of such goods or merchandise during the previous year; and

(b) a deduction of an amount equal to five per cent of the amount by which the export turnover of such goods or merchandise during the previous year exceeds the export turnover of such goods or merchandise during the immediately preceding year.

(2)(a) This section applies to all goods or merchandise [other than those specified in clause (b) if the sale proceeds of such goods or

merchandise exported out of India are receivable by the assessee in convertible foreign exchange.

(b) The goods or merchandise referred to in clause (a) are the following, namely :-

(i)agricultural primary commodities, not being produce of plantation;

(ii)mineral oil;

(iii)minerals and ores; and

(iv)such other goods or merchandise as the Central Government may, by notification in the Official Gazette, specify in this behalf."

9.On a plain reading, it becomes apparent that, in case of an assessee who exports out of India during the previous year any goods or merchandise to which the section applies, the assessee would become entitled to deductions at specified rates while computing total income of the assessee. Under sub-section (2) of Section 80HHC of the Act, it is provided under clause (a) that the section applies

to all goods or merchandise [other than those specified in clause (b)] if the sale proceeds of such exports are receivable by the assessee in convertible foreign exchange. The Tribunal has found, as a matter of fact, that, in the present case, all other conditions for being entitled to deduction under Section 80HHC of the Act, stand satisfied, and the only dispute between the parties is, whether the goods exported by the assessee are or are not “agricultural primary commodities”, which phrase appears in sub-clause (i) of clause (b) of sub-section (2) of Section 80HHC of the Act. In other words, the scheme of the section is that an assessee is entitled to deduction in relation to all goods or merchandise exported out of India except the enumerated items in clause (b) of sub-section (2) of section 80HHC of the Act.

10. The Tribunal accordingly formulated the crucial question which fell for its decision, i.e. whether HPS groundnuts come within the ambit of the expression “agricultural primary commodities” in Section 80HHC(2)(b)(i) of the Act. If the revenue

is able to show that HPS groundnuts fall within the meaning of the said expression, then the assessee would not be entitled to deduction under Section 80HHC (1) of the Act, and on the other hand, if HPS groundnuts are not “agricultural primary commodities”, then the assessee would be entitled to the deduction.

11.The expression “agricultural primary commodities” has not been defined in the Act. However, the phrase envisages that there should be an agricultural commodity, and further, it should a primary commodity. The term “agricultural” denotes that the commodity in question is a produce of agricultural operations. To that extent, there is a consensus amongst parties. The real lis is whether HPS groundnuts can be termed to be “primary commodity”. According to revenue, HPS groundnuts remained groundnuts and hence, they are “primary commodities” obtained after agricultural operations on land. The Tribunal has held that, for a commodity to be a primary commodity, it should not have been obtained after processing. In other

words, the commodity which is the produce of the land on which agricultural operations are carried out, would be a primary commodity till the point of time it is not processed further. Once the commodity undergoes a process or processes, it ceases to be primary commodity though it may continue to remain an agricultural commodity.

12.The Tribunal has recorded that the processes which are undertaken by the assessee and the commodity which is exported by the assessee as a consequence of such processes, results in the commodity ceasing to be “agricultural primary commodity”. For recording this finding, the Tribunal has appreciated the evidence on record and recorded the following findings of fact.

> “6. As far as HPS groundnuts which are exported by the assessee are concerned, admittedly they are HPS groundnut kernels. The groundnuts in shell are decorticated mechanically to remove the shell and its seeds (kernels) then pass through mechanical sieve shaker fitted with

> different graded sieves for receiving Small Seeds and foreign matter. The required graded kernels are then collected and further sorted and graded manually by experienced workers (mainly women) using sieves as per required specification. The sound kernels, after being tested for ascertaining absence of aflatoxins are then exported. These facts which were placed before the learned Commissioner were not disputed and are supported by relevant certificates produced by the assessee. It is obvious that the commodities that are exported are not agricultural primary commodities. Agricultural primary commodities are groundnuts in shell. The kernels that are ultimately exported are obtained after processing and as a result of the said processing, they cease to be agricultural primary commodities. Consequently, deduction u/s 80HHC(1) would be allowable."

13. As already noticed hereinbefore, the provision does not require that the commodity, namely, the goods which are exported ceased to be agricultural commodities. The only prohibition or exception

carved out qua the goods or merchandise which are exported is that such goods should not be “agricultural primary commodities”. In the case of Commissioner of Income Tax v. Cynamid India Ltd. (supra), the Apex Court was called upon to determine the meaning of the term “product of agriculture” as used in Section 35C of the Act. The commodity in question before the Apex Court was husk of rice which remains after de-husking of paddy. The Apex Court accepted the finding of the High Court that the operation of de-husking paddy is not an industrial or manufacturing operation as commonly understood; it is essentially an agricultural operation and such changes as are brought about in the product are an outcome of agricultural operation. Both rice and husk remain in their natural form as a result of de-husking and are covered by the term “agricultural product”. Thereafter, the Apex Court goes on to hold that: *“The term `agricultural product' or `product of agriculture' is required to be construed liberally so as to include not merely the primary product as it actually grows, but also a product which undergoes a simple operation so as to make it more*

saleable or more usable. The rice and the husk though separated remain as they were produced and hence continue to be `agricultural product' or `product of agriculture'.".

14.Hence, it can be concluded that a primary product is, as it actually grows, and on the other hand, a product which undergoes a simple operation so as to make it more saleable or more usable does not cease to be a product of agriculture. For the purpose of determining whether the present assessee's case is covered by the exclusionary clause or not, what is required to be determined is, whether the exported goods i.e. HPS groundnuts are primary commodities? Even if HPS groundnuts continue to remain agricultural commodities, whether they continue to be primary commodities or not, has to be determined. Applying the aforesaid ratio of the Apex Court, one can say that considering the process reproduced and recorded by the Tribunal, the goods in question are not in the form as actually grown and hence, cease to be a primary commodity.

15.The issue can be approached from a slightly different angle. What would be the approach of the person concerned, namely, the trader, and how would the commodity in question be treated in market, are the questions which will give an indication as to whether the commodity retains its nature of being an agricultural primary commodity. Considering the process involved in treating the unshelled groundnut before it attains the form of HPS groundnuts, namely, the kernels or the seeds, it is abundantly clear that neither the agriculturists nor the traders would regard it as a primary commodity. The test for determination as to whether manufacture can be said to have taken place or not may also usefully be invoked. In other words, whether the commodity which is subjected to the process can be regarded as the original commodity, or is it recognized in the trade as a new and distinct commodity. Does the original commodity after suffering the process experience a change, or a series of changes, so as to take the commodity to the point where commercially it is recognized as a new and distinct

article from that of the original commodity. This is the test which has been applied by the Apex Court in the case of Aspinwall & Co. Ltd. (supra) while determining whether conversion of raw berries into coffee beans would amount to a manufacturing activity within the meaning of the provisions of Section 32A of the Act. After setting out nine processes in curing of the coffee, the Apex Court has held that, after processing the raw berries, the assessee converts them into coffee beans which is commercially a different commodity.

16. Applying the aforesaid test, it is apparent that, in the present case, the assessee acquires unshelled groundnuts which are then processed and the end-product namely, groundnuts cease to be “agricultural primary commodity”, even if they continue to remain agricultural commodity, because when raw berries after processing can be termed to be manufacture of coffee beans, then in the present case, it can be stated with added emphasis that the commodity ceases to be a primary commodity. It is not disputed on behalf of the revenue that HPS

groundnuts in the form in which they are exported are commercially a different commodity. What is submitted is that, groundnuts retain their characteristics as groundnuts and hence, they are “agricultural primary commodities”. For the reasons stated hereinbefore, it is not possible to accept the contention for the simple reason that, whether the characteristics remain same or not, what is material is that the commodity ceases to be a primary commodity and is known as a commercially different product.

17.It is necessary to take note of the fact that the aforesaid view was also expressed by the High Court of Hyderabad in the case of Kishenlal Oil Mills, Hyderabad v. Commissioner of Sales Tax, Hyderabad, [1955] 6 STC 650 in context of Rule 5 of the Hyderabad Sales Tax Rules, which levied tax on various goods purchased by a dealer, one of the goods being groundnut. It was observed: “In this view of the matter, the word “ground-nut” for the purpose of sub-section (2) of rule 5, in our view, would be the unshelled ground-nut produced by the

agriculturists and not the kernel. ... ... Whenever the word “ground-nut” is used, it generically connotes to the mind the pod or unshelled ground-nut rather than the “singhdana” as opposed to “mungphalli” (unshelled ground-nut). If it was intended that the purchase turnover not only of the unshelled ground-nut but also of kernel should be liable to sales tax, it could have been easily specified by including the kernel as has been done in the case of cotton which was to include kapas.”

18.Therefore, the view adopted by the Tribunal that “agricultural primary commodities” are groundnuts in shell and the kernels that are ultimately exported after processing of groundnuts would cease to be “agricultural primary commodities”, cannot be faulted with. The Tribunal was, therefore, justified in holding that HPS groundnuts exported by the assessee did not come within the ambit of expression “agricultural primary commodities” appearing in Section 80HHC(2)(b)(i) of the Act, and that, the assessee was entitled to deduction under

Section 80HHC of the Act. The question in each of the three references is accordingly answered in the affirmative i.e. in favour of the assessee and against the revenue. All the three references stand disposed of accordingly.

19. Before parting, it is necessary to record that the paper-book supplied to the Court contained various and innumerable printing errors. Henceforth, in case such errors are not taken care of by the applicant concerned, costs may be levied on the applicant concerned in each reference.

[D.A.MEHTA, J.]

[HARSHA DEVANI, J.]

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